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IN THE

Supreme Court of the United States

October Term, ~~1948~~ 1949

No. ~~[redacted]~~ 59 59

REO MOTORS, INC.,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT AND BRIEF IN SUPPORT OF PETITION.

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COMMISSIONER OF INTERNAL REVENUE,
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PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT AND BRIEF IN SUPPORT OF PETITION.

To the Honorable, the Chief Justice and the Associate Justices of the Supreme Court of the United States:

The petition of Reo Motors, Inc. respectfully prays for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit to review a judgment of that Court entered in this case on November 29, 1948 and upon which a petition for rehearing was overruled by an order of the Court entered on the 1st day of February, 1949; and therefore shows as follows:

I.

A summary and short statement of the matter involved.

This action involves the petitioner's United States income and excess profits tax liability for the calendar year 1942. The United States Court of Appeals for the Sixth

Circuit affirmed (R. p. 216) a decision favorable to the respondent in The Tax Court of the United States (R. p. 201).

The facts in this case were stipulated. The facts essential and relevant to an understanding of the nature of the controversy and of the question involved on appeal are as follows:

The petitioner, a corporation, was organized on January 2, 1940, under the laws of the State of Michigan (Stipulation, paragraphs First and Sixth, R. pp. 54, 55). It is engaged in the trade or business of manufacturing motor vehicles (Stipulation, paragraph Thirty-fifth, R. p. 62).

In January, 1940, the petitioner acquired all of the shares of stock of Reo Sales Corporation (hereinafter referred to as Reo Sales), a corporation (Stipulation, paragraph Twelfth, R. p. 56), and a sales agent for the petitioner (Stipulation, paragraph Thirty-fifth, R. p. 62). Thereafter, until the dissolution of Reo Sales, all of its stock was owned directly by the petitioner (Stipulation, paragraph Twelfth, R. p. 56). Petitioner's adjusted basis for determining gain or loss from the sale or other disposition of the stock of Reo Sales was $1,551,902.79 (Stipulation, paragraph Fifteenth, R. p. 57).

On February 1, 1941, Reo Sales was indebted to the petitioner in the sum of $1,263,707.57. During the calendar year 1941, Reo Sales was dissolved and as of February 1, 1941, all of its assets, subject to all its liabilities, were transferred to the petitioner. The net value of such assets was $1,048,219.95 (Stipulation, paragraph Fourteenth, R. p. 57).

The loss sustained by the petitioner on the dissolution of Reo Sales was not compensated for by insurance or otherwise. The loss with respect to the stock of Reo Sales was a long-term capital loss under the law applicable to the

taxable year 1941 (Stipulation, paragraph Sixteenth, R. p. 57). It was so claimed by the petitioner in its return for 1941 and allowed by the respondent (Exhibit A annexed to the Petition and Amended Petition, R. pp. 17, 43; Stipulation, paragraph Third, R. p. 55).

For the petitioner's taxable year 1941, its gross income was $2,573,259.89 (Stipulation, paragraph Twenty-second, R. p. 59). The deductions allowable to the petitioner by Chapter 1 of the Internal Revenue Code (not including any deduction with respect to the stock of Reo Sales, any deduction for depletion, any net operating loss deduction, or any deduction for losses from sales or exchanges of capital assets) were $2,215,727.08 (Stipulation, paragraphs Seventeenth, Nineteenth, Twentieth and Thirty-fourth, R. pp. 58, 59).

For the taxable year 1942 the net income of the petitioner, without the allowance of a net operating loss deduction and without the allowance of any deduction for depletion, was $1,926,136.34 (Stipulation, paragraphs Twenty-fourth and Twenty-fifth, R. p. 59). The petitioner's normal tax net income, computed without the allowance of a net operating loss deduction, without the allowance of any deduction for depletion and without the credit provided in section 26(e) of the Internal Revenue Code, was $1,926,102.34 (Stipulation, paragraphs Twenty-fourth, Twenty-fifth, and Twenty-eighth, R. pp. 59, 60).

In computing its income and excess profits tax liability for the year 1942 the petitioner claimed as a deduction allowable under section 23(s) of the Internal Revenue Code a net operating loss deduction (R. pp. 124, 143, 163). Upon audit of the petitioner's tax return for the year 1942, the respondent determined that the loss sustained by the petitioner in 1941 on the worthlessness in that year of the

stock of the Reo Sales must be eliminated in the determination of the amount of a net operating loss deduction allowable for the year 1942, and as a result of that determination, together with other adjustments which are not in dispute, the respondent recomputed the petitioner's income for the year 1942, in which recomputation no net operating loss deduction was allowed (R. pp. 14-22).

II.

A statement particularly disclosing the basis upon which it is contended that the Supreme Court of the United States has jurisdiction to review the judgment of the United States Court of Appeals for the Sixth Circuit.

(a) The statutory provision believed to sustain the jurisdiction of the Supreme Court of the United States.

The Supreme Court of the United States has jurisdiction to review the judgment of the United States Court of Appeals by reason of the provisions of Section 1254 of Title 28 of the United States Code (Public Law 773—80th Congress, Chapter 646, 2d Session).

(b) The date of the judgment sought to be reviewed and the date upon which the petition for a writ of certiorari is presented.

(1) The date of the judgment sought to be reviewed is November 29, 1948 (R. p. 216). A petition for rehearing thereon was overruled by an order of the United States Court of Appeals for the Sixth Circuit on February 1, 1949 (R. p. 235).

(2) The date upon which the petition for a Writ of Certiorari is presented is April 25, 1949.

III.

The question presented.

The question presented is as follows:

Is the petitioner, in computing its tax liability for the year 1942, entitled to include in determining its net operating loss deduction allowable for 1942 the loss sustained by it in the year 1941 by reason of the worthlessness in that year of the stock of Reo Sales Corporation?

IV.

The reasons relied on for the allowance of the writ.

The decision herein of the United States Court of Appeals for the Sixth Circuit is in conflict, both in result and theory, with the decision of the United States Court of Appeals for the Fifth Circuit in *Commissioner of Internal Revenue* v. *Moore, Inc.* (151 F. (2d) 527, aff'g 4 T. C. 404). Further, the United States Court of Appeals for the Sixth Circuit has decided an important question of federal law which has not been, but should be, settled by the Supreme Court of the United States.

1. In the *Moore, Inc.* case, as in the instant case, the issue before the Court was the determination of the taxpayer's tax liability for the year 1942, the specific question in each case being the amount, if any, of the net loss deduction allowable in 1942 under sections 23(s) and 122 of the Internal Revenue Code (Title 26 of the United States Code) on account of a net loss sustained in 1941. In both cases, if the law applicable to 1942 was determinative, the taxpayer was entitled to a net loss deduction in computing its 1942 tax liability. On the other hand, if the law, as it existed in 1941, was applicable, the taxpayer in neither case would be entitled to the deduction. In both cases, the change in

the law between 1941 and 1942 was effected by the Revenue Act of 1942 (Public Law No. 753, 77th Congress, 2d Session) and by section 101 of that Act was made "applicable only with respect to taxable years beginning after December 31, 1941."

In the *Moore, Inc.* case, both The Tax Court of the United States and the United States Court of Appeals for the Fifth Circuit held that since the question in issue was the determination of tax liability for 1942, the law applicable to the year 1942 governed and that the taxpayer was entitled to recover. In the instant case, the United States Court of Appeals for the Sixth Circuit held that the law applicable to 1941 and not 1942 governed and that the taxpayer was not entitled to recover. The basic conflict between the two theories applied in the two cases is illustrated by the diametrically opposed interpretations of the provisions of section 101 of the Revenue Act of 1942 which states:

> "Except as otherwise expressly provided, the amendments made by this title shall be applicable only with respect to taxable years beginning after December 31, 1941."

In its opinion in the *Moore, Inc.* case, The Tax Court said (4 T. C. 404, 406):

> "Certainly, in its present context, 'with respect to' could mean nothing less than 'in computing a tax liability for.' Thus, paraphrasing section 101, *supra*, section 122(d)(4) of the Internal Revenue Code, as amended by section 150(e) of the Revenue Act of 1942, the provision would read 'shall be applicable * * * in computing a tax liability for taxable years beginning after December 31, 1941.' The question here is the tax liability of petitioner for such a year —the calendar year 1942. * * *"

In affirming the decision of The Tax Court, the United States Court of Appeals for the Fifth Circuit said (151 F. (2d) 527, 528):

> "And we are not left to conjecture as to when the amendment was to become effective, for the amending Act, at the beginning of Part I, Title 1, which consists of amendments to the Revenue Code, declares in Sect. 101, 56 Stat. 802, 26 U. S. C. A. Int. Rev. Acts, 'Except as otherwise expressly provided, the amendments made by this title shall be applicable only with respect to taxable years beginning after December 31, 1941.' There is no 'otherwise' provision. So this amendment applies with respect to taxable years beginning after December 31, 1941. It therefore applies with respect to the taxable year 1942. It is with respect to taxation for that year that the carry-over produced by a capital loss is here claimed as a deduction; and to ascertain what if anything is deductible by way of carry-over from 1941, we think, as did the Tax Court, that by the express words of the amended Section 122(d)(4), 'gains and losses from sales or exchanges of capital assets shall be taken into account' without any reference to what sort of result would have been figured out in 1941 under the then law. * * * "

In striking contrast to the foregoing statements, the United States Court of Appeals for the Sixth Circuit said in the instant case (R. p. 220):

> "It is contended that the taxpayer's liability for 1942, computed under the 1942 Amendment, requires the use of a formula given by the 1942 Act to compute the amount of the net operating loss for 1941, which, however, has nothing to do with the tax liability for 1941. This result is reached by pointing out that the words in Sec. 101 of the Revenue Act of 1942 reading 'shall be applicable only with respect to taxable years beginning after December 31, 1941'

means the same thing as 'shall be applicable only in computing a tax liability for taxable years beginning after December 31, 1941.' The argument might have some merit if the words of the statute are so changed, but we are not authorized to change them, and we believe there is a substantial difference between the phrase 'with respect to' as it stands in the statute and the phrase 'in computing a tax liability for' as urged by Petitioner. * * * "

In its opinion in this case, The Tax Court attempted to distinguish the *Moore, Inc.* case on the ground that there an amendment to section 122(d)(4) of the Internal Revenue Code was involved, whereas here, the amendment was to section 23(g)(4). However, as pointed out in the opinion of the United States Court of Appeals herein (R. p. 220), the respondent has specifically conceded that the two cases are not properly distinguishable. The fact is that in both cases, the loss involved could be excluded in the computation of the net operating loss deduction only through the operation of section 122(d)(4) of the Internal Revenue Code. In the *Moore, Inc.* case, there was involved a change in the language of section 122(d)(4) itself, whereas in the instant case, the definition of a term used in section 122(d)(4) was changed in section 23(g)(4). The distinction suggested by The Tax Court is that if "with respect to" 1942 a word in section 122(d)(4) is changed, such amendment is effective in the computation of 1942 tax liability, whereas, if the definition of a term appearing in section 122(d)(4) is changed in another section also "with respect to" 1942, the amendment is not applicable in the computation of 1942 tax liability. The difference between the two cases is manifestly inconsequential and the cases are not distinguishable.

2. The basic issue involved in the instant case is whether the law applicable to 1941 or the law applicable to 1942 is determinative in the computation of the petitioner's

1942 tax liability. The determination of that issue is dependent, in part at least, upon the interpretation of section 101 of the Revenue Act of 1942 which provides:

> "Except as otherwise expressly provided, the amendments made by this title shall be applicable only with respect to taxable years beginning after December 31, 1941."

The use of the words "with respect to taxable years beginning after" a particular date is not unique in section 101 of the Revenue Act of 1942 but represents the general method used by Congress in specifying the effective date of amendments to the Internal Revenue Code. See for example, section 229 of the Revenue Act of 1939, Public Law No. 155, 76th Congress, Chapter 247, 1st Session; sections 105 and 203 of the Revenue Act of 1948, Public Law No. 471, 80th Congress, Chapter 168, 2d Session. Consequently, the decision below in the instant case involves an important question of federal law, not limited in its application to the years 1941 and 1942 or to the specific questions presented in this case or in the *Moore, Inc.* case, but which is applicable to other years as well and to other situations where an event occurring in one taxable year has an effect upon the computation of tax liability for a subsequent or prior taxable year. We submit that the importance of the question and the general applicability of the principle involved require a determination by this Court.

WHEREFORE, your petitioner respectfully prays that a Writ of Certiorari be issued out of and under the seal of this honorable Court directed to the United States Court of Appeals for the Sixth Circuit, commanding that court to certify and send to this Court for its review and determination, on a day certain to be therein named, a full and com-

plete transcript of the record and all proceedings in this cause to the end that the said cause may be reviewed and determined by this Court according to law; and that your petitioner may have such other and further relief as to this Court may seem proper and in conformity with law.

And your petitioner will ever pray.

JAMES O. WYNN,
N. BARR MILLER,
Attorneys for Petitioner.

Dated: April 22, 1949.

PETITIONER'S BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

Opinions of the Courts Below.

The opinion of the United States Court of Appeals for the Sixth Circuit is reported in 170 F. (2d) 1001 (see pp. 216-223 of the Record). The opinion of The Tax Court of the United States is reported in 9 T. C. 314 (see pp. 191-200 of the Record).

Jurisdiction.

The grounds on which the jurisdiction of the Supreme Court of the United States is invoked are set forth beginning at page 4 herein, in the Petition for Writ of Certiorari.

Statement of the Case.

The facts are as set forth, beginning at page 1 herein, in the Petition for Writ of Certiorari.

Specification of Errors.

1. The United States Court of Appeals for the Sixth Circuit erred in determining that the loss of $1,551,902.79 sustained by the petitioner in the year 1941 by reason of the worthlessness in that year of the stock of Reo Sales Corporation should be excluded in determining the amount of the net operating loss deduction allowable as a deduction for the year 1942 under the provisions of sections 23(s) and 122 of the Internal Revenue Code.

2. The United States Court of Appeals for the Sixth Circuit erred in finding in its opinion that the provisions of section 23(g) of the Internal Revenue Code, as that sec-

tion was constituted in 1941, are applicable in determining whether a loss sustained in 1941 (on the worthlessness of stock in that year) may be included in the determination for the year 1942 of the amount of the net operating loss deduction (computed in accordance with section 122 of the Internal Revenue Code, as that section was constituted in 1942, and allowable as a deduction for the year 1942 under section 23(s) of the Internal Revenue Code).

3. The United States Court of Appeals for the Sixth Circuit erred in failing to find that the provisions of section 23(g) of the Internal Revenue Code, as that section was constituted in 1942, are applicable in determining whether a loss sustained in 1941 (on the worthlessness of stock in that year) may be included in the determination for the year 1942 of the amount of the net operating loss deduction (computed in accordance with section 122 of the Internal Revenue Code, as that section was constituted in 1942, and allowable as a deduction for the year 1942 under section 23(s) of the Internal Revenue Code).

4. The United States Court of Appeals for the Sixth Circuit erred in affirming the decision of The Tax Court of the United States wherein it ordered and decided that there are deficiencies in the petitioner's income tax and excess-profits tax in the respective amounts of $565,971.65 and $268,655.14 for the calendar year 1942.

5. The United States Court of Appeals for the Sixth Circuit erred in entering judgment for the respondent.

Summary of the Argument.

The petitioner sustained a loss of $1,551,902.79 in the year 1941 upon the worthlessness in that year of the stock of Reo Sales Corporation. The issue here in dispute in

volves the petitioner's income and excess-profits tax liability for the year 1942. The petitioner's tax liability for the year 1942 must be computed in accordance with the provisions of the Internal Revenue Code applicable to the year 1942. Under the provisions of section 23(g)(4) of the Internal Revenue Code, applicable to the year 1942, the loss on the worthlessness of the stock of Reo Sales Corporation was an ordinary, not a capital, loss. Such loss, therefore, is not to be eliminated in computing the amount of petitioner's net operating loss deduction for the year 1942 under section 122 of the Internal Revenue Code.

ARGUMENT.

There is no dispute over the fact that in the year 1941 the petitioner sustained a loss of $1,551,902.79 by reason of the worthlessness in that year of the stock of Reo Sales Corporation. Section 23(g) of the Internal Revenue Code, applicable to the year 1941, provided, so far as material here, that a loss resulting from the worthlessness of securities (including shares of stock in a corporation) should "be considered as a loss from the sale or exchange, on the last day of such taxable year, of capital assets". Therefore, the loss sustained by the petitioner on the worthlessness of the Reo Sales Corporation stock was a long-term capital loss for the purpose of computing the petitioner's tax liability for the year 1941, and there is no disagreement between the parties on that point.

However, the petitioner's tax liability for the year 1941 is not in issue nor of any importance in determining the question presented. The question in controversy involves solely the petitioner's tax liability for the year 1942 and, specifically, whether in determining its tax liability for the

year 1942, the petitioner is entitled to a deduction under section 23(s) of the Internal Revenue Code which provides:

> "*Net Operating Loss Deduction.*—For any taxable year beginning after December 31, 1939, the net operating loss deduction computed under section 122."

Section 122 of the Internal Revenue Code is a complex section setting forth the manner in which the deduction allowed under section 23(s) shall be computed.[1] The computation of the net operating loss deduction involves the determination of net operating losses, net operating loss carry backs and carry-overs and, finally, the amount of the net operating loss deduction itself.

The starting point is whether there is an "excess of the deductions allowed by this chapter over the gross income". In the instant case, the taxpayer had for the year 1941 an excess of allowable deductions over its gross income, regardless of whether the provisions of the Internal Revenue Code, as they existed in 1941 or in 1942, are applied. As previously mentioned, the loss which the petitioner sustained on the worthlessness of the stock of Reo Sales Corporation was under the provisions of section 23(g) of the Internal Revenue Code as it existed in 1941, a long-term capital loss. Section 23(g) of the Internal Revenue Code was amended by section 123(a) of the Revenue Act of 1942 by adding thereto a new subparagraph (4) to exclude from

[1] Section 122 of the Internal Revenue Code was extensively amended by the Revenue Act of 1942. For the convenience of the Court, the provisions of section 122 as they appeared before amendment are set forth in Appendix A hereto, and as they appeared after amendment in Appendix B hereto.

the classification of capital assets stock in affiliated corporations.[2]

Regardless of which law is considered effective, the loss on the Reo Sales Corporation stock was an allowable deduction and the excess of the deductions allowed over the gross income would be identical in either case.[3]

This case, therefore, does not involve a situation where a loss or expenditure constituted an allowable deduction under the law applicable to one year but not under the law applicable to the other. Up to this point, therefore, there is no need to determine which law is applicable; the result will be identical in either case.

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[2] Section 23(g)(4) provides:

"(4) *Stock in Affiliated Corporation*—For the purposes of paragraph (2) stock in a corporation affiliated with the taxpayer shall not be deemed a capital asset. For the purposes of this paragraph a corporation shall be deemed to be affiliated with the taxpayer only if:

"(A) at least 95 per centum of each class of its stock is owned directly by the taxpayer; and

"(B) more than 90 per centum of the aggregate of its gross incomes for all taxable years has been from sources other than royalties, rents (except rents derived from rental of properties to employees of the company in the ordinary course of its operating business), dividends, interest (except interest received on deferred purchase price of operating assets sold), annuities, or gains from sales or exchanges of stocks and securities; and

"(C) the taxpayer is a domestic corporation."

Facts have been stipulated showing that Reo Sales was affiliated with the taxpayer within the requirements of the foregoing section. (Stipulation, paragraphs First, Twelfth and Thirteenth, R. pp. 54, 56-57.)

[3] Under the law applicable to 1941, the full amount of the loss was allowable as a deduction without limitation in computing income for 1941 since it constituted a long-term capital loss (section 117(d) of the Internal Revenue Code as it existed in 1941).

The determination of an excess of deductions allowed over gross income is, however, only the starting point. Adjustment must be made for the "exceptions, additions and limitations provided in subsection (d)" of section 122 of the Internal Revenue Code.

Of the exceptions, additions and limitations provided in subsection (d) of section 122, the only one which could have any possible application is that appearing in subparagraph (4) of section 122(d). Section 122(d)(4) as it read prior to amendment by the Revenue Act of 1942 provided:

> "Long-term capital gains and long-term capital losses shall be taken into account without regard to the provisions of section 117(b). As so computed the amount deductible on account of long-term capital losses shall not exceed the amount includible on account of the long-term capital gains, and the amount deductible on account of short-term capital losses shall not exceed the amount includible on account of short-term capital gains."

Section 150(e) of the Revenue Act of 1942 amended section 122(d)(4) to read as set forth below:

> "Gains and losses from sales or exchanges of capital assets shall be taken into account without regard to section 117(b). As so computed the amount deductible on account of such losses shall not exceed the amount includible on account of such gains; * * * "

Section 101 of the Revenue Act of 1942 provides:

> "Except as otherwise expressly provided, the amendments made by this title shall be applicable only with respect to taxable years beginning after December 31, 1941."

Neither section 123(a) of the Revenue Act of 1942 which added subparagraph (4) to section 23(g) of the Internal

Revenue Code nor section 150(e) of the Revenue Act of 1942 amending section 122(d)(4) of the Internal Revenue Code contains any provisions with respect to the effective date thereof. Consequently, both sections were subject to section 101 of the Revenue Act of 1942, and by that section made "applicable only with respect to taxable years beginning after December 31, 1941".

The terms "long-term capital gains"; "long-term capital losses", "short-term capital losses", "short-term capital gains" and "gains and losses from sales or exchanges of capital assets" are given specific definitions in the Internal Revenue Code (sections 23(g) and 117). Consequently, when these words are used in the statute, they must be given the well defined meaning which Congress has assigned to them. By section 123(a) of the Revenue Act of 1942 amending section 23(g) of the Internal Revenue Code, Congress specifically provided that stock in an affiliated corporation (as there defined) shall not constitute a capital asset. ~~It is~~ inescapable therefore, we submit, that when in section 150 (e) of the same Revenue Act of 1942 (amending section 122 (d)(4) of the Code) Congress used the term "capital assets", it intended that that term did not include stock in an affiliated corporation. Where a term has once been defined, it is unnecessary to repeat that definition whenever such term is again used in the statute; the use of the term itself is equivalent to a repetition of the definition. Section 23 (g)(2) of the Internal Revenue Code, to which section 23 (g)(4) specifically relates, sets forth a rule "for the purposes of this chapter". Since section 122 of the Internal Revenue Code is a part of the same chapter, the definition in section 23(g)(4) necessarily applies to section 122(d)(4).

It is clear, therefore, we submit, that if in determining 1942 tax liability the exceptions, additions and limitations required to be made in determining the amount of the 1942

deduction must be computed in accordance with the provisions of the Internal Revenue Code specifically made applicable with respect to the year 1942, section 122(d)(4) of the Internal Revenue Code as it existed in 1942, and not as it existed in some prior year, must be applied. If section 122(d)(4) of the Internal Revenue Code, as it existed in 1942, is applied in this case, it will follow automatically that the deduction which the petitioner has claimed is proper and allowable.

In *Moore, Inc.* v. *Commissioner* (4 T. C. 404, aff'd 151 F. (2d) 527), the specific question involved was whether section 122(d)(4) of the Internal Revenue Code as it existed in 1942, or as it existed in 1941, was to be applied in computing the taxpayer's tax liability for the year 1942. Both The Tax Court of the United States and the United States Court of Appeals for the Fifth Circuit held that section 122(d)(4) of the Internal Revenue Code as it existed in 1942 was to be applied.

The Tax Court of the United States in its opinion in that case pointed out that the question before it was the tax liability of a taxpayer for the calendar year 1942 and said:

> "The answer to that question requires the use of a formula to compute the amount of the net operating loss for 1941. But the use of that formula has nothing to do with the tax liability for 1941. Its use here is limited to the determination of the tax liability of petitioner for the calendar year 1942."

The Tax Court of the United States was unquestionably correct in its observation that the use of a formula was required and that the formula had nothing to do with 1941 tax liability. A taxpayer may have a tremendous net loss in one year, but after going through the computations required under section 122 of the Internal Revenue Code to determine if he has a deduction in a subsequent year, may find

that he has no net operating loss or net operating loss deduction whatsoever. On the other hand, it seems possible that, under particular circumstances, a taxpayer may have a net taxable income for one year upon which he is required to pay a tax and still find that he has a net operating loss deduction in the succeeding year.[4]

The basis upon which The Tax Court of the United States decided the *Moore, Inc.* case is clearly set forth in its opinion as follows (4 T. C. 404, 406):

> "Section 101 of 'Title I—Individual and Corporation Income Taxes' of the Revenue Act of 1942 bears the subtitle 'Taxable Years to Which Amendments

[4] For example, assume that in 1942 an individual, who had no income in 1941, had gross business income of $5,000 and business deductions of $6,000, that he realized a profit of $10,000 on the sale of capital assets held for less than six months and that he also sustained a loss of $10,000 on the sale of capital assets held for more than six months. For the year 1942, the taxpayer had net *taxable* income of $4,000 upon which he was required to pay a tax. (The gain of $10,000 on the sale of capital assets held for less than six months is includible in income in full, but only 50% of the loss sustained on the sale of securities held for more than six months may be deducted. (Section 117(b) of the Internal Revenue Code.) The taxpayer thus would have a net gain of $5,000 to report on his security transactions. Deducting from this the net loss of $1,000 sustained in his business would leave the taxpayer with a net income of $4,000.) There were no changes in the law between 1942 and 1943 which could have any bearing upon the example given and, thus, in determining whether the taxpayer has a net operating loss carryover from 1942 to 1943, it is immaterial whether the 1942 or 1943 law is considered applicable. Under section 122(d)(4) of the Internal Revenue Code applicable to both years, gains and losses from sales or exchanges of capital assets shall be taken into account without regard to the provisions of section 117(b) and the full amount of the profits and losses on the sale of securities would be taken into account in determining whether the taxpayer had a net operating loss in 1942. The $10,000 of losses would, thus, cancel out the $10,000 of gain, leaving a net loss of $1,000 from the operation of the business as a net operating loss for 1942, assuming that no further adjustments are required for percentage depletion, etc. Thus, the taxpayer, although having a net income for 1942, upon which he is required to pay a tax, may, nevertheless, be considered as having sustained a net operating loss in that year which may be carried forward as a deduction in computing 1943 income.

Applicable.' It reads: 'Except as otherwise expressly provided, the amendments made by this title shall be applicable only with respect to taxable years beginning after December 31, 1941.'

"Section 150(e) of the Revenue Act of 1942, *supra*, amending subsection (d)(4) of section 122 of the Internal Revenue Code, contains no express provision as to the time that amendment is to become effective.

"Certainly, in its present context, 'with respect to' could mean nothing less than 'in computing a tax liability for.' Thus, paraphrasing section 101, *supra*, section 122(d)(4) of the Internal Revenue Code, as amended by section 150(e) of the Revenue Act of 1942, the provision would read 'shall be applicable * * * in computing a tax liability for taxable years beginning after December 31, 1941.' The question here is the tax liability of petitioner for such a year —the calendar year 1942. The answer to that question requires the use of a formula to compute the amount of the net operating loss for 1941. But the use of that formula has nothing to do with a tax liability for 1941. Its use here is limited to the determination of the tax liability of petitioner for the calendar year 1942.

"We conclude, therefore, that the 'net operating loss' of petitioner for 1941, to be used in the computation of its net operating loss carry-over to the calendar year 1942 for determining its net income and taxes for that latter year, shall be computed under section 122(d)(4) of the Internal Revenue Code, as amended by section 150(e) of the Revenue Act of 1942."

The identical reasoning was adopted in the opinion of the United States Court of Appeals for the Fifth Circuit in which it was said (151 F. (2d) 527, 528):

"And we are not left to conjecture as to when the amendment was to become effective, for the amend-

> ing Act, at the beginning of Part I, Title 1, which consists of amendments to the Revenue Code, declares in Sect. 101, 56 Stat. 802, 26 U. S. C. A. Int. Rev. Acts, 'Except as otherwise expressly provided, the amendments made by this title shall be applicable only with respect to taxable years beginning after December 31, 1941.' There is no 'otherwise' provision. So this amendment applies with respect to taxable years beginning after December 31, 1941. It therefore applies with respect to the taxable year 1942. It is with respect to taxation for that year that the carry-over produced by a capital loss is here claimed as a deduction; and to ascertain what if anything is deductible by way of carry-over from 1941, we think, as did the Tax Court, that by the express words of the amended Section 122(d)(4), 'gains and losses from sales or exchanges of capital assets shall be taken into account' without any reference to what sort of result would have been figured out in 1941 under the then law. * * * "

In the instant case, the United States Court of Appeals for the Sixth Circuit has adopted a directly contrary view. It is stated in the opinion of that Court (170 F. (2d) 1001, 1004; R. p. 219) that the *Moore, Inc.* case involved section 122(d)(4) of the Internal Revenue Code, whereas here, we are concerned with section 23(g)(4). This statement overlooks completely the fact that the only issue in this case, as in the *Moore* case, is whether an adjustment is required under section 122(d)(4), and that when Congress in section 122(d)(4) used the term "capital assets" it was necessarily using that term as it is defined in sections 23(g)(4) and 117.

The Court below, in effect, concedes that if the provision in section 101 of the Revenue Act of 1942 that the amendments "shall be applicable only with respect to taxable years beginning after December 31, 1941" is interpreted as it was in the *Moore, Inc.* case to mean nothing less than

"in computing a tax liability for" taxable years beginning after December 31, 1941, the position of the petitioner here would be correct. The Court stated (R. p. 220):

> "* * * The argument might have some merit if the words of the statute are so changed, but we are not authorized to change them, and we believe there is a substantial difference between the phrase 'with respect to' as it stands in the statute and the phrase 'in computing a tax liability for' as urged by Petitioner. It is true that in the present case we are not computing a tax liability for 1941, but if we make the 1942 Amendment applicable to the transaction in 1941 we are making it applicable 'with respect to' a transaction in the taxable year 1941 contrary to the provisions of the amendment."

The Court, without attempting to offer any interpretation of the words "with respect to" in section 101 of the Revenue Act of 1942, has attempted to write into the statute a limitation to the effect that the amendment can have no application to an event occurring prior to the effective date thereof, regardless of whether the tax liability in question is for a period prior to, or subsequent to, such effective date, and regardless of the effect which such event may have "with respect to" the subsequent period. The fact is, however, that the statute does not refer to transactions occurring in any period. The statute directs itself *to* taxable *years*. There is nothing to indicate that Congress in any way had in mind *events* occurring *in* any particular period of time. We submit that when in a revenue statute Congress makes an amendment applicable "with respect to" a taxable year, the language, in the words of The Tax Court in the *Moore, Inc.* case, "could mean nothing less than 'in computing a tax liability for' ". It may be suggested that the words "with respect to" are not the same words as "in

computing a tax liability for" and that if Congress had intended the latter, it could have so stated. The fact is that the words "with respect to" are broad and general and more inclusive than the words "in computing a tax liability for". We suggest that Congress used the broad and general words deliberately but not as an indication of intent that the amendment should not be applicable in computing tax liability for the year to which the amendment was made applicable. The use of the words "in computing a tax liability for" alone would be inadequate. The provisions of the Internal Revenue Code are not directed solely to the computations of tax liability. The essential function of the Internal Revenue Code is to provide a method for the computation of tax liability, but the Code encompasses much more. For example, it provides methods for the payment and enforcement of the tax liability (sections 51-60, 141-151), for statutes of limitations upon the assessment and refund of taxes (sections 275-277, 322), penalties for evasion of the tax (section 145) and many other related matters. It would, therefore, be inaccurate for Congress to provide that the amendments contained therein shall be applicable only in the computation of the tax liability for a particular year when such amendments relate to matters other than the mere computation of tax liability.

For example, section 136 of the Revenue Act of 1942 amended section 51 of the Internal Revenue Code to remove the requirement that individual tax returns be filed under oath and substituted therefor a requirement that there be a written declaration that the return is made under the penalties of perjury. No specific provision was made for the effective date of this amendment and it was, therefore, by the terms of section 101 of the Revenue Act of 1942 made "applicable only with respect to taxable years beginning after December 31, 1941". That amendment had nothing

to do with the computation of tax liability as such. Other amendments, however, were of importance only in connection with the computation of tax liability, as for example, section 103 of the Revenue Act of 1942 amending section 12(b) of the Internal Revenue Code providing for the rates of surtax. We submit, therefore, that when Congress provides that amendments to the Internal Revenue Code "shall be applicable only with respect to taxable years beginning after" a particular date, Congress intends that the amendments shall be given the broadest possible application in connection with any matters affecting taxable years beginning after the date specified. Since some of the amendments are of importance only in connection with the computation of tax liability, the words "with respect to" must necesarily include the sense of "in computing a tax liability for"; although the words "with respect to" can, and should, be interpreted as encompassing more than a mere "in computing a tax liability for", such words cannot properly be given a meaning excluding "in the computation of tax liability for".

The Court below argues (R. p. 221) that if Congress had intended the result for which the petitioner contends "Congress could have given section 23(g)(4) retroactive application by expressly providing that it should be applicable to transactions in preceding years in cases where a tax liability was being computed for taxable years beginning after December 31, 1941, involving transactions in such prior years". Of course, Congress could have used the words suggested. Also, it could, instead of the broad and general words "with respect to", have used the specific words necessary to make it clear in exactly what sense the amendments effected by sections 102 and 103 of the Revenue Act of 1942 dealing with tax rates, section 136(a) dealing with the signing of returns, section 136(b) dealing with penalties

or any other section should be applicable "with respect to taxable years beginning after December 31, 1941". That Congress believed that the words suggested by the Court below were unnecessary and were included in the broad and general term is demonstrated by the Report of the Senate Finance Committee (Senate Report No. 1631, 77th Congress, Second Session) (discussed *infra*, p. 27).

The Court below suggests (R. p. 220) that the interpretation urged by the petitioner, and adopted by both The Tax Court of the United States and the United States Court of Appeals for the Fifth Circuit in the *Moore, Inc.* case, would make the 1942 amendment applicable "with respect to" a transaction in the taxable year 1941. The petitioner does not contend, and never has contended, that the 1942 amendment could in any way affect the manner or the extent to which the 1941 transaction was to affect its 1941 tax liability. The petitioner does contend, however, that the manner and the extent to which a transaction occurring in 1941 shall be reflected in its 1942 tax return and affect its tax liability for 1942 must be determined under the law specifically made applicable "with respect to" the taxable year 1942.

A familiar situation in which a transaction occurring in one taxable year affects the tax liability of a future taxable year is where a taxpayer sells property on the installment plan and in accordance with the provisions of section 44 of the Internal Revenue Code elects to report his profit on the installment basis. The sale may or may not have constituted the sale or exchange of a capital asset under the law applicable to the year of sale. However, the character of the income, whether capital gain or ordinary income, to be reported with respect to such sale in a subsequent year is governed by the law in effect during such subsequent year and not by the law in effect during the year of sale. (*Snell* v. *Com'r*, 97 F. (2d) 891; *Hay* v. *Com'r*,

25 B. T. A. 96; Example I of Section 29.117-7 of Regulations 111.) [5]

The Court below dismissed the argument based upon the *Snell* and *Hay* cases and Section 29.117-7 of Regulations 111 by the observation (R. p. 222) that "such subsequent installment payments are properly governed by the law of the year in which received. The Regulation deals with a situation entirely different from the one here involved". We submit that the two situations are not entirely different. In both cases, there is a transaction in one year which affects the tax liability of a subsequent year. In the one case, the taxpayer sells property at a profit which need not be included in full in income in the year of sale but may be deferred to a future period. In the other case, a loss is sustained which, with the other deductions allowable, exceeds the net income for the year of loss and the question is the carry-over of such loss to the succeeding year. If, in the one case, the character of the income to be included in the later year is to be determined by whether the law of the later year defines the property sold in the earlier year as a capital asset, why should not the character of the loss to be carried over to the later year likewise be determined by the law applicable to the later year? In each case, the transaction giving rise to the gain or loss occurred in the prior year and did, or did not, constitute a sale or exchange of a capital asset under the law applicable to such earlier year. However, in neither

[5] Section 151(b) of the Revenue Act of 1942 added subsection (j) to section 117 of the Internal Revenue Code and by section 101 of the Revenue Act of 1942 (the identical section applicable to the amendments to sections 122(d) and 23(g)(4) of the Code) the amendment was made "applicable only with respect to taxable years beginning after December 31, 1941". The example of the Regulations cited shows that in the case of a sale in 1941 (not resulting in a capital gain under the law applicable to that year) the profit to be reported in 1942 may be reported as a capital gain under section 117(j).

case are we concerned with the taxpayer's tax liability for the earlier year. We submit that in both cases the taxpayer's tax liability for the later year must be determined in accordance with the provisions of law made applicable "with respect to" the later year and not by what the law may have provided in the earlier period.

The correctness of the position contended for by the petitioner here and adopted by The Tax Court of the United States and the United States Court of Appeals for the Fifth Circuit in the *Moore, Inc.* case is demonstrated by the Report of the Senate Finance Committee on the Revenue Bill of 1942. The Senate Finance Committee proposed an amendment to the Revenue Bill of 1942 as passed by the House. Section 155 of the Senate Finance Committee Bill (section 153 of the Bill as finally enacted [6]) amended, among other things, section 122(b) of the Internal Revenue Code to provide for a different definition of a net operating loss carryover than had theretofore been contained in the Code. The amendments proposed by the Committee were expressly made applicable only to taxable years beginning after December 31, 1940. In its Report with respect to this amendment, the Senate Finance Committee stated (Senate Report No. 1631, 77th Congress, Second Session, p. 123; Cumulative Bulletin 1942-2, p. 596):

> "The net operating loss deduction for any taxable year is the sum of the carry-backs and the carry-overs to such taxable year. The amendments made by this section *are applicable to all taxable years beginning after December 31, 1940.* Thus, in the case of a taxpayer on the calendar year basis, *the carry-overs to the taxable year 1941 from the taxable years*

[6] Section 153 of the Revenue Act of 1942 as adopted is reproduced in Appendix C hereto.

> *1939 and 1940*, and the carry-backs to such taxable year from the taxable years 1942 and 1943 *will be determined under the amendments made by this section.*" (Italics supplied.)

Thus, there was a specific recognition by the Congressional Committee that the amendment although applicable only "to all taxable years beginning after December 31, 1940" would be effective in determining the carry-overs to the taxable year 1941 from the taxable years 1939 and 1940. The Court below (R. p. 221) completely misconceived the significance of this Report. Section 153 of the Revenue Act of 1942 did *not* merely add a provision permitting net operating loss carry-backs. Subsection (b) of that section did amend the prior law to permit carry-backs as well as carry-overs. However, subsection (a) of the section deals with the manner of computing the *amount* of a carry-back or carry-over. Under section 153(c) of the Revenue Act of 1942 amending section 122(e) of the Code, no carry-back is permitted to years prior to 1941. Accordingly, the amount of any carry-overs from 1939 and 1940 to 1941 could not in any way be influenced by carry-backs from subsequent years. It is obvious, therefore, that when the Committee referred to carry-overs from 1939 and 1940 to 1941 being determined under the amendments, it was *not* referring to the amendments effected by section 153(b) of the Revenue Act of 1942 providing for carry-backs.

As mentioned above, subsection (a) of section 153 of the Revenue Act of 1942 deals with the manner of computing the amount of carry-overs and carry-backs. Subsection (b) of section 122 of the Internal Revenue Code, as it previously existed, was amended by being subdivided into two subparagraphs, subparagraph (1) being concerned with net operating loss carry-backs and subparagraph (2) being concerned with net operating loss carry-overs. In this con-

nection, the Senate Finance Committee (Senate Report No. 1631, 77th Congress, Second Session, p. 122; Cumulative Bulletin 1942-2, p. 596) said:

> "The *amount* which may be carried back or carried forward is limited in the case of each such preceding or succeeding year to the amount which was not used to offset income for any taxable years before such preceding or succeeding year. In determining the *amount* of the net operating loss which is so used to offset income in any taxable year, the net income for such taxable year is computed without the deduction of any carry-over or carry-back from the year in which the net operating loss arose or from any year subsequent thereto *but with certain other adjustments now required under section 122(d)*. The net operating loss which is a carry-over or a carry-back to such taxable year is considered to have been applied against the net income so computed." (Italics supplied.)

As stated by the Senate Finance Committee, the amount of a net loss must be reduced by the amount of the net income of an intervening year "but with certain other adjustments now required under section 122(d)". Obviously, the Committee was referring to that part of section 122(b)(2), as amended by section 153(a) of the Revenue Act of 1942, providing that the amount of a net operating loss should be reduced by the amount of the income of the intervening taxable year computed "with the exceptions, additions, and limitations provided in subsection (d)(1), (2), (4), and (6)".

A comparison of section 122(b) before and after amendment (see Appendices A and B) shows that the amended section requires an adjustment under section 122(d)(6), whereas, no such adjustment was required before amendment.

The Senate Finance Committee did not state merely that in computing income for a year beginning after December 31, 1940 the net loss deduction would be the sum of carry-backs and carry-overs. It went on to say that such carry-backs and carry-overs "will be determined under the amendments made by this section" specifically stating that any carry-overs to the taxable year 1941 from the taxable years 1939 and 1940 would be determined under the amendment.

When in section 153 of the Revenue Act of 1942 Congress amended the method of computing net loss carry-overs and provided that the amendments effected by that section would be applicable only to taxable years beginning after December 31, 1940 and the Senate Finance Committee specifically stated that the carry-overs to the taxable year 1941 from the taxable years 1939 and 1940 would be determined under the amendments, there was a clear recognition that making the amendments applicable to the year 1941 was making the amendments applicable in the computation of tax liability for the year 1941.

Further, the position taken by the Senate Finance Committee is diametrically opposed to the position upon which the respondent has built the foundation for his entire argument. The basic premise upon which the respondent has argued this case is that the amount of the net operating loss is determined by reference to the law applicable to the year of loss, the net operating loss carry-over by reference to the law applicable to the intervening year and only the net operating loss deduction itself by the law applicable to the year of deduction. Thus, the effect of respondent's argument is that in determining whether a taxpayer is entitled to take a net operating loss deduction in 1941 by reason of a net loss in 1939, the net operating loss is to be computed under the law applicable to 1939, the net operat-

ing loss carry-over under the law applicable to 1940 and only the adjustments thereto to determine a net operating loss deduction under the law applicable to 1941. Yet, the Senate Finance Committee stated that such was not the case. It stated that the net operating loss carry-over was to be determined by an amendment applicable only to 1941 and subsequent years, that is, that the law applicable to 1941, and not the law applicable to 1940, was to govern the determination of the net operating loss carry-over. Thus, the foundation itself for the respondent's argument is removed.

The concept of the allowance of a deduction for the losses of one year from the gross income of another first appeared in the Revenue Act of 1924. These provisions of the Revenue Act of 1924 were reenacted in the Revenue Acts of 1926, 1928 and 1932. As set forth in the Revenue Act of 1932, the provisions were repealed as of January 1, 1933 by section 218(a) of the National Industrial Recovery Act (June 16, 1933). As pointed out in the opinion of The Tax Court in the *Moore, Inc.* case, each one of these revenue acts contained a provision to the effect that the net loss to be carried forward from one year to a succeeding taxable year was to be computed under the law applicable to the earlier year.

When, after a lapse of six years, Congress reinstituted the principle of the carry-over of a net loss as a deduction in a subsequent year, the Internal Revenue Code was amended by section 211(b) of the Act of June 29, 1939 by the additions of section 23(s) and 122. It is apparent that the language of the prior revenue acts was borrowed liberally in section 122. However, the provisions of the prior acts to the effect that the law applicable to the prior year was to be applied in determining the amount of the net loss to be carried forward were omitted. This omission was taken by The Tax Court in its opinion in the *Moore* case

as an indication that Congress did not intend to have the law of the prior year apply, a position supported by the familiar principle that some significance must be attached to the omission of words in the reenactment of a statute. As was said in *Pirie* v. *Chicago Title & Trust Co.* (182 U. S. 438, 448):

> "The words in italics are omitted from the act of 1898. Was the omission without purpose? The omission of a condition is certainly not the same thing as the expression of a condition. Was it left out in words to be put back by construction? Taken from the certainty given by prior use and prior decisions, and committed to doubt and controversy? There is a presumption against it. When the purpose of a prior law is continued, usually its words are, and an omission of the words implies an omission of the purpose. This rule we lately applied in *Bardes* v. *First Nat. Bank*, 178 U. S. 524, 44 L. ed. 1175, 20 Sup. Ct. Rep. 1000. In that case, in determining whether the jurisdiction of the circuit and district courts of the United States was concurrent with the state courts in certain suits at law and equity between the assignee in bankruptcy and the adverse claimant of property of the bankrupt, the statutes of 1841 and 1867 were compared with that of 1898, and from the omission from the latter of certain provisions of the former statutes it was decided that such jurisdiction did not exist. It was said by the court, speaking by Mr. Justice GRAY: 'We find it impossible to infer that when Congress, in framing the act of 1898, entirely omitted any similar provision, and substituted the restricted provisions of § 23, it intended that either of those courts should retain the jurisdiction which it had under the obsolete provision of the earlier acts.'"

The fact that Congress in other provisions of the Internal Revenue Code has made it clear when the provisions

of prior law are to control is an indication that Congress had no such intention in the present case. For example, section 113(a)(3) of the Internal Revenue Code provides:

> "The basis of property shall be the cost of such property; except that—
>
> • • • • • • •
>
> (3) Transfer In Trust After December 31, 1920.—If the property was acquired after December 31, 1920, by a transfer in trust (other than by a transfer in trust by a gift, bequest, or devise) the basis shall be the same as it would be in the hands of the grantor increased in the amount of gain or decreased in the amount of loss recognized to the grantor upon such transfer *under the law applicable to the year in which the transfer was made.*" (Italics supplied.)

Language similar to the italicized portion of section 113 (a)(3) as quoted above will be found in subsections (a)(5), (6), (7), (8), (9) and (13) of section 113 of the Internal Revenue Code.

Certainly, there is no basis of principle for determining that the amount to be allowed as a net operating loss deduction in one year shall be determined by reference to the law of a prior year. The history of the various revenue acts and of the Internal Revenue Code itself is obviously an evolution based upon experience. From time to time, experience has shown that, for example, a deduction theretofore allowed in the computation of gross income should not be allowed, or that a deduction not theretofore allowed should be allowed. Experience has further shown from time to time that a change previously made was too sweeping in its application, and an exception should be made. When these things have become apparent, Congress has amended the law to correct the previous error. Although, as a matter of principle, these amendments should perhaps

be made retroactive, that would involve the reopening of tax liabilities previously considered as settled and cause great inconvenience and confusion to both the Treasury and taxpayers. Consequently, such amendments are ordinarily made applicable only with respect to taxable years in which the change is made and subsequent years.

Originally, a capital gain or loss occurred only upon the sale or exchange of a capital asset.[7] Thus, if a taxpayer sold a security for $1.00 for which he had paid $100, his loss of $99 constituted a capital loss. However, if he did not sell the security, but it became worthless, his loss then was not a capital loss but an ordinary loss. By section 23(g) of the Revenue Act of 1938 (Public Law No. 554, 75th Congress, 3d Session), the law was amended to provide that the loss sustained upon the worthlessness of shares of stock should be considered as a capital loss. This was later considered to be too sweeping a change, and in recognition of the fact that a loss sustained on the worthlessness of the stock of an affiliated company was in the nature of a business rather than an investment loss, the law was again

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[7] In the Report of the House Committee on Ways and Means on the Revenue Bill of 1938 (Report No. 1860, 75th Congress, 3d Session) it was said (p. 18):

"Under section 23(e) of the Revenue Act of 1936 a loss sustained from securities becoming worthless which is deductible under that subsection is deductible in full and against ordinary income. In contrast thereto a loss sustained from the sale or exchange of such securities as are capital assets is not only subject to reduction by the percentage brackets of section 117(a) of that act but cannot be offset against ordinary income except to the extent of $2,000. This distinction in treatment is not satisfactory, since, in either case, the loss sustained by the taxpayer is a loss of capital and consequently should be treated similarly for tax purposes. This difference in treatment is eliminated by the bill. Section 23(g) thereof, dealing with capital losses, subjects losses arising from stock or stock rights becoming worthless to the same limitations provided under section 117 of the bill with respect to sales or exchanges."

amended by the 1942 Act by the addition of subsection (4) of section 23(g). Thus, in 1942, Congress recognized that the loss on the worthlessness of the stock of an affiliated company should not be treated as a capital loss and subject to the various limitations placed thereon.

Since the amendment was made effective with respect to taxable years beginning after December 31, 1941, and we are here concerned with the taxpayer's tax liability for the year 1942, we submit that, as a matter of principle, the taxpayer's tax liability for 1942 should be computed in the manner in which Congress then deemed that losses occasioned by the worthlessness of the stock of an affiliated company should be treated. To adopt the respondent's position would be to perpetuate and to carry over into 1942 a concept of the nature of a loss sustained on the worthlessness of the stock of an affiliate, which Congress found, by the amendment to section 23(g)(4), was no longer appropriate.

The Court below (R. p. 221) stated that "Under petitioner's construction of section 101 the net operating loss in any given year would not be a fixed quantity but with changes in the taxing act would vary from year to year." No reason is given why a net operating loss should be a static amount and we submit there is none. The fact that a taxpayer may have a net operating loss in 1941 under the law applicable to 1941 does not guarantee to the taxpayer the allowance of that net operating loss as a deduction in 1942. Congress may, in the law applicable to 1942, completely deny any deduction therefor, or may provide that the deduction shall be in an amount quite different than that computed under the prior law. What Congress considers in 1942 to be the proper amount is the amount to be allowed as a deduction in computing 1942 tax liability and not what may have been considered the proper amount

in 1941. Further, we submit that no considerations of administrative difficulty require that a net operating loss be a static amount. Section 122 of the Internal Revenue Code is a complex section but, we submit, the difficulties inherent in the application of that section would not be increased whether the petitioner's or the respondent's theory is sustained. It is perhaps possible to conjecture a theoretical set of facts, very unlikely to happen, under which there might be some administrative inconveniences. Certainly, however, no administrative difficulty is involved in this case, in the *Moore, Inc.* case or in any case reasonably likely to happen. We submit that the basis of reason and principle should not be discarded because of the remote possibility that in a few possible but unlikely cases there may be some slight measure of administrative inconvenience. Further, whatever administrative inconvenience might be found in some unlikely case under the petitioner's theory would be matched under the respondent's theory by the inconvenience that in some equally remote situation it would be necessary to apply the laws applicable to five different taxable years to the determination of the tax liability for a single year.

Conclusion.

It is, therefore, respectfully submitted that the Petition for Writ of Certiorari should be granted as prayed for.

Respectfully submitted,

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Appendix A.

Section 122 of the Internal Revenue Code as it Read Prior to Amendment by the Revenue Act of 1942.

Sec. 122. Net operating loss deduction.

Sec. 122(a). Definition of net operating loss.—As used in this section, the term "net operating loss" means the excess of the deductions allowed by this chapter over the gross income, with the exceptions and limitations provided in subsection (d).

Sec. 122(b). Amount of carry-over.—The term "net operating loss carry-over" means in the case of any taxable year the sum of:

Sec. 122(b)(1). The amount, if any, of the net operating loss for the first preceding taxable year; and

Sec. 122(b)(2). The amount of the net operating loss, if any, for the second preceding taxable year reduced by the excess, if any, of the net income (computed with the exceptions and limitations provided in subsection (d)(1), (2), (3), and (4) for the first preceding taxable year over the net operating loss for the third preceding taxable year.

Sec. 122(c). Amount of net operating loss deduction.—The amount of the net operating loss deduction shall be the amount of the net operating loss carry-over reduced by the amount, if any, by which the net income (computed with the exceptions and limitations provided in subsection (d) (1), (2), (3), and (4)) exceeds, in the case of a taxpayer other than a corporation, the net income (computed without such deduction), or, in the case of a corporation, the normal-tax net income (computed without such deduction);

Sec. 122(d). Exceptions and limitations.—The exceptions and limitations referred to in subsections (a), (b), and (c) shall be as follows:

Sec. 122(d)(1). The deduction for depletion shall not exceed the amount which would be allowable if computed

without reference to discovery value or to percentage depletion under section 114(b)(2), (3), or (4);

Sec. 122(d)(2). There shall be included in computing gross income the amount of interest received which is wholly exempt from the taxes imposed by this chapter, decreased by the amount of interest paid or accrued which is not allowed as a deduction by section 23(b), relating to interest on indebtedness incurred or continued to purchase or carry certain tax-exempt obligations;

Sec. 122(d)(3). No net operating loss deduction shall be allowed;

Sec. 122(d)(4). Long-term capital gains and long-term capital losses shall be taken into account without regard to the provisions of section 117(b). As so computed the amount deductible on account of long-term capital losses shall not exceed the amount includible on account of the long-term capital gains, and the amount deductible on account of short-term capital losses shall not exceed the amount includible on account of the short-term capital gains;

Sec. 122(d)(5). Deductions otherwise allowed by law not attributable to the operation of a trade or business regularly carried on by the taxpayer shall (in the case of a taxpayer other than a corporation) be allowed only to the extent of the amount of the gross income not derived from such trade or business. For the purposes of this paragraph deductions and gross income shall be computed with the exceptions and limitations specified in paragraphs (1) to (4) of this subsection.

Sec. 122(e). No carry-over from year prior to 1939. As used in this section, the terms "third preceding taxable year", "second preceding taxable year", and "first preceding taxable year" do not include any taxable year beginning prior to January 1, 1939.

Appendix B.

Section 122 of the Internal Revenue Code as it Read After Amendment by the Revenue Act of 1942.

Sec. 122. Net operating loss deduction.

Sec. 122(a). Definition of net operating loss.—As used in this section, the term "net operating loss" means the excess of the deductions allowed by this chapter over the gross income, with the exceptions, additions and limitations provided in subsection (d).

Sec. 122(b). Amount of carry-back and carry-over.—

Sec. 122(b)(1). Net operating loss carry-back.—If for any taxable year beginning after December 31, 1941, the taxpayer has a net operating loss, such net operating loss shall be a net operating loss carry-back for each of the two preceding taxable years, except that the carry-back in the case of the first preceding taxable year shall be the excess, if any, of the amount of such net operating loss over the net income for the second preceding taxable year computed (A) with the exceptions, additions, and limitations provided in subsection (d)(1), (2), (4), and (6), and (B) by determining the net operating loss deduction for such second preceding taxable year without regard to such net operating loss.

Sec. 122(b)(2). Net operating loss carry-over.—If for any taxable year the taxpayer has a net operating loss, such net operating loss shall be a net operating loss carry-over for each of the two succeeding taxable years, except that the carry-over in the case of the second succeeding taxable year shall be the excess, if any, of the amount of such net operating loss over the net income for the intervening taxable year computed (A) with the exceptions, additions, and limitations provided in subsection (d)(1), (2), (4), and (6), and (B) by determining the net operating loss deduction for such intervening taxable year without regard to such net

operating loss and without regard to any net operating loss carry-back. For the purposes of the preceding sentence, the net operating loss for any taxable year beginning after December 31, 1941 shall be reduced by the sum of the net income for each of the two preceding taxable years (computed for each such preceding taxable year with the exceptions, additions, and limitations provided in subsection (d)(1), (2), (4), and (6), and computed by determining the net operating loss deduction without regard to such net operating loss or to the net operating loss for the succeeding taxable year).

Sec. 122(c). Amount of net operating loss deduction.— The amount of the net operating loss deduction shall be the aggregate of the net operating loss carry-overs and of the net operating loss carry-backs to the taxable year reduced by the amount, if any, by which the net income (computed with the exceptions and limitations provided in subsection (d)(1), (2), (3), and (4) exceeds, in the case of a taxpayer other than a corporation, the net income (computed without such deduction) or in the case of a corporation, the normal-tax net income (computed without such deduction and without the credit provided in section 26(e));

Sec. 122(d). Exceptions, additions and limitations.— The exceptions, additions, and limitations referred to in subsections (a), (b), and (c) shall be as follows:

Sec. 122(d)(1). The deduction for depletion shall not exceed the amount which would be allowable if computed without reference to discovery value or to percentage depletion under section 114(b)(2), (3), or (4);

Sec. 122(d)(2). There shall be included in computing gross income the amount of interest received which is wholly exempt from the taxes imposed by this chapter, decreased by the amount of interest paid or accrued which is not allowed as a deduction by section 23(b), relating to interest on indebtedness incurred or continued to purchase or carry certain tax-exempt obligations;

Sec. 122(d)(3). No net operating loss deduction shall be allowed;

Sec. 122(d)(4). Gains and losses from sales or exchanges of capital assets shall be taken into account without regard to the provisions of section 117(b). As so computed the amount deductible on account of such losses shall not exceed the amount includible on account of such gains;

Sec. 122(d)(5). Deductions otherwise allowed by law not attributable to the operation of a trade or business regularly carried on by the taxpayer shall (in the case of a taxpayer other than a corporation) be allowed only to the extent of the amount of the gross income not derived from such trade or business. For the purposes of this paragraph deductions and gross income shall be computed with the exceptions, additions, and limitations specified in paragraphs (1) to (4) of this subsection.

Sec. 122(d)(6). There shall be allowed as a deduction the amount of tax imposed by Subchapter E of Chapter 2 paid or accrued within the taxable year, subject to the following rules—

(A) No reduction in such tax shall be made by reason of the credit for income, war-profits, or excess-profits taxes paid to any foreign country or possession of the United States;

(B) Such tax shall be computed without regard to the adjustments provided in section 734; and

(C) Such tax, in the case of a consolidated return for excess-profits tax purposes, shall be allocated to the members of the affiliated group under regulations prescribed by the Commissioner, with the approval of the Secretary.

Sec. 122(e). No carry-back to year prior to 1941.—As used in this section, the term "preceding taxable year" and the term "preceding taxable years" do not include any taxable year beginning prior to January 1, 1941.

Appendix C.

Section 153 of the Revenue Act of 1942

Sec. 153. Two-Year Carry-Back of Net Operating Losses.

(a) *Determination of Carry-Back.*—Section 122(b) (relating to the amount of the net operating loss carry-over), is amended to read as follows:

"(b) *Amount of Carry-Back and Carry-Over.*—

"(1) *Net Operating Loss Carry-Back.*—If for any taxable year beginning after December 31, 1941, the taxpayer has a net operating loss, such net operating loss shall be a net operating loss carry-back for each of the two preceding taxable years, except that the carry-back in the case of the first preceding taxable year shall be the excess, if any, of the amount of such net operating loss over the net income for the second preceding taxable year computed (A) with the exceptions, additions, and limitations provided in subsection (d) (1), (2), (4), and (6), and (B) by determining the net operating loss deduction for such second preceding taxable year without regard to such net operating loss.

"(2) *Net Operating Loss Carry-Over.*—If for any taxable year the taxpayer has a net operating loss, such net operating loss shall be a net operating loss carry-over for each of the two succeeding taxable years, except that the carry-over in the case of the second succeeding taxable year shall be the excess, if any, of the amount of such net operating loss over the net income for the intervening taxable year computed (A) with the exceptions, additions, and limitations provided in subsection (d) (1), (2), (4), and (6), and (B) by determining the net operating loss deduction for such intervening taxable year without

regard to such net operating loss and without regard to any net operating loss carry-back. For the purposes of the preceding sentence, the net operating loss for any taxable year beginning after December 31, 1941 shall be reduced by the sum of the net income for each of the two preceding taxable years (computed for each such preceding taxable year with the exceptions, additions, and limitations provided in subsection (d) (1), (2), (4), and (6), and computed by determining the net operating loss deduction without regard to such net operating loss or to the net operating loss for the succeeding taxable year)."

(b) *Amount of Net Operating Loss Deduction.*—Section 122(c), relating to the amount of the net operating loss deduction, is amended by inserting in lieu of "amount of the net operating loss carry-over" the following: "aggregate of the net operating loss carry-overs and of the net operating loss carry-backs to the taxable year".

(c) Section 122(e) is amended to read as follows:

"(e) *No Carry-Back to Year Prior to 1941.*—As used in this section, the term 'preceding taxable year' and the term 'preceding taxable years' do not include any taxable year beginning prior to January 1, 1941."

(d) *Limitation on Interest on Overpayment Caused by a Carry-Back of Loss or Credit.*—Section 3771 (relating to interest on overpayments) is amended by inserting at the end thereof the following:

"(e) *Claims Based on Carry-Back of Loss or Credit.*—If the Commissioner determines that any part of an overpayment is attributable to the inclusion in computing the net operating loss deduction for the taxable year of any part of the net operating loss for a succeeding taxable year or to the inclusion in computing the unused excess profits credit adjust-

ment for the taxable year of any part of the unused excess profits credit for a succeeding taxable year, no interest shall be allowed or paid with respect to such part of the overpayment for any period before the filing of a claim for credit or refund of such part of the overpayment or the filing of a petition with the Board, whichever is earlier."

(e) *Effective Date.*—The amendments made by this section shall be applicable only to taxable years beginning after December 31, 1940.

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